

***United States Court of Appeals
for the Second Circuit***



**APPELLANT'S
BRIEF**

77-1140

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

DOCKET NO. 77-1140

B
P/S

UNITED STATES OF AMERICA,

Appellee,

v.

EDWIN J. SCHULZ,

Appellant.

BRIEF FOR APPELLANT EDWIN J. SCHULZ

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Dated: May 9, 1977

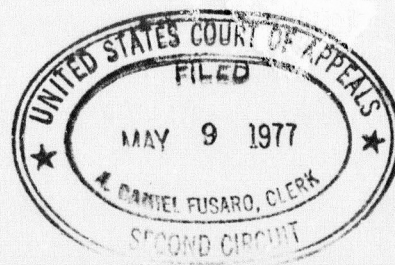


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Preliminary Statement

Edwin J. Schulz appeals from a judgment of conviction entered on March 11, 1977 in the U.S. District Court for the Southern District of New York after a six-week trial before the Honorable Marvin E. Frankel, U.S. District Judge, and a jury. Indictment 76 Cr. 685, filed July 27, 1976, charged five former officers of the Stirling Homex Corporation with fraud in the sale of Homex stock. The trial of all five defendants began on December 22, 1976. On January 29, 1977 the jury

found each of the defendants guilty on all counts. On March 11, 1977 Judge Frankel fined Schulz \$2,500, placed him on probation for one year, and suspended imposition of any further sentence. The other four defendants received substantial jail sentences.

Issues Presented

1. Should Schulz' grand jury testimony, made in connection with an offer to plead guilty, have been suppressed pursuant to Rule 11 (e) (6) of the Federal Rules of Criminal Procedure?

2. Should certain of the indictment's specifications against Schulz, supported by insufficient evidence, have been withdrawn from the jury's consideration?

STATEMENT OF FACTS

Stirling Homex Corporation, formed in 1968 near Rochester, N.Y., was a pioneer in the business of manufacturing and installing factory-built housing. Homex had public stock offerings in February 1970 and July 1971, after reporting substantial "book" profits. In July 1972, Homex was placed in bankruptcy by its creditor banks, and it is still in the process of liquidation.

Schulz was hired as Comptroller in September 1968. when the company was very small. He reported to Richard Karkow, Executive Vice President in charge of finance. Schulz' participation in the 1970 public offering was minimal. In February 1971, after plans were underway for the second offering, Karkow abruptly resigned. Schulz was given Karkow's responsibility for supplying the financial information for the second offering. Schulz was not a certified public accountant, and was characterized by an important government witness as "over his head" in the world of corporate finance. (Tr.3019-20) In August 1971, shortly after the second offering, he was replaced as Comptroller and was given the title of Vice President of Operations. (Tr. 3312) He stopped working for Homex in April 1972, and returned home to Lancaster, Pennsylvania. (Tr.3732)

Schulz testified at length during investigations by the Trustee in Bankruptcy and the Securities and Exchange Commission. In January and February of 1976, he was interviewed on five different days by the Assistant U.S. Attorney in charge of the case, W. Cullen MacDonald. In March 1976, MacDonald advised Schulz that he was going to recommend Schulz' indictment.

Subsequently Schulz and his attorney, George Miller of the Pennsylvania bar, entered into plea negotiations with MacDonald. On July 15, 1976 Schulz and MacDonald concluded a written plea agreement. It stated, among other things, that the Government would accept a guilty plea to one count of conspiracy, on the condition that Schulz would testify before the grand jury. Schulz testified before the grand jury on the following day. About a month after the indictment, he decided to withdraw from his plea agreement.

Prior to trial, Schulz moved to suppress his grand jury testimony pursuant to Rule 11(e)(6) of the Federal Rules of Criminal Procedure, on the ground that it was made in connection with an offer to plead guilty. Judge Frankel initially denied the motion without a hearing on November 5, 1976. Schulz then moved for reconsideration. On January 6, 1977, a hearing was held at which Schulz testified. (Tr. 2009-2033) Judge Frankel again denied the motion. (Tr. 2037-2041)

The Government then read to the jury portions of Schulz' grand jury testimony. (GX 381; Tr. 2496-98, 2606-10, 3382-86) This testimony was clearly the strongest evidence against Schulz.

The indictment contained nine counts -- charging fraud in the sale of securities (Count One), false statements in the

1971 registration statement (Count Two), mail fraud (Count Three through Eight), and conspiracy (Count Nine). However, all nine counts were identical in their essential specifications. These specifications were contained in Paragraphs 10 through 16 of Count One, which were incorporated by reference in each of the other counts. Judge Frankel correctly instructed the jury that these were "seven key paragraphs which play, over and over again, the central role really in each of the nine counts." (Tr.5979)

The indictment named Schulz as a criminal participant under each of these specifications except Paragraph 16. Paragraph 15 (a) was tailored to one of Schulz' grand jury admissions. As to the other specifications, on all but one the evidence against Schulz was clearly insufficient.

At the end of the Government's case, Schulz, by oral and written motions and by a request to charge, asked that particular specifications be withdrawn from jury consideration, on the ground of insufficiency of evidence. The motions and request were denied.

GOVERNMENT'S CASE

A. Land Sales to Kece and Raseac (Indictment, ¶¶ 10 and 11)

In 1969 Homex sold two separate parcels of land to two

corporations named Kece and Raseac. Although Homex received only 10% down payments, it recorded the entire amount of its expected profits in its "book" profits for the fiscal year ending July 31, 1969. The Government objected to this bookkeeping on the ground that there were secret oral promises guaranteeing the purchasers against loss.

The purchasers testified that they received such oral promises, but only in the presence of two defendants, David Stirling Jr. and Harold Yanowitch. There was no evidence that Schulz participated in arranging either of these two land sales, or that he had any knowledge of the oral agreements. Of course, Schulz recorded these sales in Homex's books, but this was in no way fraudulent in the absence of such knowledge.

B. Land Sale to Route 57 & 31 Development Corp.
(Indictment, ¶12)

In 1971 Homex sold a parcel of land to a corporation named Route 57 & 31 Development Corporation. Again, although Homex received only a 10% down payment, it recorded the entire amount of its expected profit in its "book" profits for the seven months ending February 28, 1971 (which was the most recent audited period for the second offering). The Government objected to this bookkeeping on two grounds: (a) again, there

were secret oral promises guaranteeing the purchasers against loss, and (b) to finance the down payment, Homex arranged a bank loan for the purchaser and deposited \$100,000 in the bank which may have served as a compensating balance. There was ample evidence of these two circumstances, but no evidence that Schulz knew about either of them.*

In connection with this sale, Homex obtained advance approval from two outside CPA's - - Dr. Joseph Mauriello (Professor of Accounting at New York University's Graduate School of Business Administration) and William Murray (a Peat Marwick partner and a specialist in real estate accounting). In fact, Mauriello and Murray told Homex how to modify the terms of the proposed sale so that the SEC would be more likely to approve the inclusion of this sale in Homex's book profits. This modification was made, but ultimately the SEC forced Homex to take this sale out of profits.

*The Government's rebuttal summation (Tr.5922-23) made the far-fetched claim that Schulz knew of the "back door" financing because, it was claimed, Schulz should have noticed the \$100,000 change in Homex's bank balances. This claim was flatly contrary to the testimony of Government witness Paul Kuveke, Homex's Treasurer, who said that he, and not Schulz' department, computed and monitored the bank balances. (Tr.1765-66) Kuveke, who was a CPA, never suspected that there was "back door" financing (See Tr.5610). Judge Frankel overruled Schulz' objection to this portion of the rebuttal summation. (Tr.5953-54) See Schulz App. 161-64.

C. Method of Recognizing Income from Sales
of Modules; "Reassignments" (Indictment, ¶13)

Paragraph 13 was one of only two specifications where the charges against Schulz were supported by sufficient evidence. However, the specification itself did not make sense, and the evidence was highly technical and debatable. Although it occupied only a small part of the trial, it will take several pages to summarize it here.

Homex was by no means a fictitious operation. It was undisputed that the Homex assembly lines manufactured thousands of high-quality "modules". (Each module was a two or three-room section of a townhouse, with a completed interior and exterior). It was also undisputed that Homex transported many of these modules to various cities and assembled them, sometimes with record-breaking speed, into completed housing developments. Most of Homex's customers were local housing authorities. The money was supplied by federal agencies. Homex was usually paid nothing until the development was completed, and the company was often short of cash; the Government never disputed that these facts were adequately disclosed.

Homex used the percentage-of-completion method of

accounting. The typical contract stated one price for manufacturing the modules and a separate price for installing them. Homex recognized the manufacturing price as "book" income well before it received any cash -- after the module was (a) manufactured and (b) assigned to a specific contract. Homex clearly stated this to the SEC. The strange specification in Paragraph 13 charged that this representation was false, although it was indisputably true. Paragraph 13 then went on to say:

"This representation was false because, as the defendants well knew, such assignments had been repeatedly cancelled or reversed, with the modules then being reassigned from project to project ***."

The fact that something is later "reassigned" cannot make it false to say that it was earlier "assigned." Thus, all of the above passage after the word "because" is a non sequitur. By written motion, Schulz contended that this was a separate reason for dismissing this specification and withdrawing it from jury consideration. (Schulz App., 138) This motion was denied.

At the trial, the Government rephrased this allegation, and argued that Homex's practices of "reassignments" violated

the principles of its "manufactured and assigned" method of accounting. In the first place, there was a question as to when a module could be said to be "assigned" or "reassigned." Prof. Mauriello testified that in his opinion, under Homex's method of accounting, the company had the right to wait until the final day of a "reporting period" (at first this was every 6 months, later every 3 months) before committing itself as to exactly which modules were assigned to which contracts. (Tr. 2637) *

In actual practice, Homex would often book a sale early in the reporting period on the basis of one contract, and then later, before the close of the reporting period, would reverse that sale and book a new sale showing the same modules assigned to a different contract. The reason for doing this was a management decision that the second contract could be completed sooner than the first -- an important consideration for a company short of cash. (Tr.4786, Schulz Exh.B-17)

Occasionally, Homex would reverse a sale after the close of a reporting period, that is, a sale which had previously

*Although Mauriello claimed he could not remember giving this opinion to Schulz (Tr.2636), Schulz said the same thing to Peat Marwick well before they made their certification (Tr.4801-02)

been reported to the SEC and the public. However, prior to the second offering, such reversals occurred seldom, and only as to a portion of a given project.

The key point was that these journal entries were never hidden from anyone. The Peat Marwick auditors saw these entries, and each entry had an explanatory foot note which clearly stated that it was a reversal. (Tr.2472-74)

Nevertheless, the Government contended that both types of reversals on the books -- whether made before or after the close of the reporting period -- were "reassignments," and that both types violated Homex's method of accounting.* Using this theory, the Government introduced a chart (GX 364) which showed that Homex "reassigned" almost 1,100 dwelling units** (worth \$13.5 million) during the four months ending February 28, 1971.

The Government then claimed that Schulz had lied in prior statements when he said that, to his knowledge, reassignments were "minor" until November 1971. (GX 381) In response, Schulz

*This Government contention was supported by the testimony of Murray (Tr. 3336,3412), Peat Marwick's "client partner," who was not a member of the audit team. The supervisor of the audit team, Woods, took a far more permissive view. (Tr.4786,4814-19)

**A "dwelling unit," which was generally a townhouse, consisted of two, three or four "modules."

introduced a chart which showed "reassignments" as Schulz understood that term -- that is, it showed only reversals of sales that had previously been reported to the SEC or the public. (Schulz Exh. A, based upon the cross-examination of the Government's chart preparer, Tr. 2549-66) There was no dispute that Schulz' chart was accurate. It showed that Schulz' prior statements were true, if one accepted his entirely plausible interpretation of the word "reassignments."

The Government also taxed Schulz with a letter to the SEC which was drafted by Murray (GX 55; Tr. 3458) and signed by Schulz under great time pressure. (Tr. 3021-22, 4792) At one point this letter stated that modules were "assigned to and reserved exclusively for that specific project." (GX 55, p.6)

The Government contended that the word "exclusively" had the connotation of "irrevocably," and that the statement was misleading because it omitted the fact that Homex sometimes reassigned modules from one project to another. A more natural interpretation of the statement would be a simple assurance that Homex never assigned one module simultaneously to two projects.*

* The statement was interpreted this way by Woods of Peat Marwick (Tr. 4818).

Mauriello emphasized to Schulz that Homex should never make such a double assignment (Tr.2626), and it never did.

Although Peat Marwick saw the journal entries, which clearly showed the reversals, the Government claimed that Peat Marwick was somehow misled by the Homex computer system which kept track of its module inventory. This computer system generated two different computer print-outs, "File 1" and "File 2". "File 1" was a working file used by the Operations Control Department, a group that coordinated between the Site Planning, Accounting and Shipping Departments. "File 1" was insanely complicated and unwieldy, partly because it was duplicative of redundant handwritten records (GX 826,GX 823, Tr.3049-50), and partly because the modules were given different serial numbers by different departments at different times (Tr.3081-85). "File 2" was prepared for one simple purpose -- for use by the auditors during their periodic physical inspection of the modules (Tr.3067-68). The initial preparation of "File 2" was ordered by Howard Byron, the head of Operations Control (Tr.3057). A courtesy copy of Byron's order was sent to Schulz (Tr.3059,GX 785).

The Government claimed that "File 1" and "File 2" were a "double set of books". However, the difference between the

two files served no devious purpose. The difference occurred when Schulz' department assigned a module to a contract for which there was only a "general" site plan. For example, this happened on all of the assignments on the huge Mississippi contract. In such a situation, "File 2" would show, for each module, the code number of its specific contract; "File 1" would not show a specific contract. (Tr. 3079-80) The key point was that Peat Marwick was fully aware that Homex was assigning hundreds of modules to the Mississippi contract on the basis of "general" site plans. (Tr. 3392) Peat Marwick's physical inspections verified that every module had really been manufactured, and that no module had been assigned to two contracts. In order to conduct these inspections, they needed a computer print-out which showed the code number for each specific contract. Obviously, "File 2" was suitable for this purpose and "File 1" was not.*

There was evidence of a deception of Harris Kerr Forster & Co., who were the auditors prior to Peat Marwick. In 1970

*Although the "File 1" print-out was never supplied to Peat Marwick, their computer experts made a lengthy study of the computer system which related to the module inventory. (Tr. 4820-22)

Harris Kerr was supplied with receipts* for modules; the dates and the numbers of modules had been altered (GX 399B). One Richard McKeown gave testimony which clearly implied that Schulz had made the alterations (Tr.3031-35). However, the cross examination of McKeown (Tr.3040-46) and handwriting comparison clearly showed that the documents had been altered by McKeown. The evidence against McKeown was analyzed in the defense summation for Schulz (Tr.5800-15). The Government's lengthy rebuttal summation made no attempt to rehabilitate McKeown's testimony.

D. Mississippi Sale Based on a Forged Letter
(Indictment, ¶14)

This incident was by far the most shocking in the entire case. In early 1971 Homex announced an enormous project in Mississippi. It was to include the building of a second plant

* These receipts were of little importance, although of course it was outrageous to alter them. The receipts, not requested after 1970, were requested by Harris Kerr because the old form of Homex contract mentioned turnover to a common carrier. It was fully understood that the common carrier, who had an office right on the Homex premises, was signing these receipts even though the modules often had not left the premises. (Tr.3037) Under Homex's method of accounting, as long as a module had been manufactured and assigned, it was irrelevant whether it had been shipped or even physically segregated; Prof. Mauriello so testified (Tr.2620-21).

in Mississippi, and the sale of 800 dwelling units for \$15 million to a number of non-profit citizens groups which were sponsoring low-income housing projects scattered throughout Mississippi. Although Homex had a \$15 million contract with Greater Gulf Coast Housing Development Corporation (an umbrella corporation for all the non-profit groups), it was worthless without a financing commitment. Prior to the second public offering, Homex included almost \$8 million in its gross income on the basis of the Mississippi sale. In justification of this, Yanowitch showed the auditors a \$15 million financing commitment on the letterhead of the Farmers Home Administration, purportedly signed by William T. Richardson.

At the trial Richardson testified that the signature was a forgery. In any event, there was no dispute that his signature was unauthorized, and therefore that the letter was invalid. Accordingly, the issue under Paragraph 14, and the most important issue in the entire case, was: Which of the defendants knew that this letter was

invalid? Paragraph 14 charged that each of the five defendants knew this.

There was no evidence that Schulz had any knowledge that the Mississippi deal was improper. Nevertheless, the Government claimed that the jury could infer such knowledge from a Schulz memorandum to Yanowitch (GX 630) which included the following sentence:

"I mentioned [to Homex attorney Jerome Dienstag] the Farmers Home Administration as being the ultimate source of funds but suggested that he discuss this with you before disclosing it to any outside parties."

The Government, both in its initial summation and in its rebuttal summation, urged Schulz' guilt under Paragraph 14 on the basis of nothing but this single sentence. (Tr. 5631-32, 5923; Schulz App. 159-60, 162)

The fact that Schulz had been told by his superior, Yanowitch, that the letter was confidential is no proof that Schulz knew the letter was improper. Moreover, Schulz had no duty to question Yanowitch. Peat Marwick did have this duty. Three Peat Marwick partners --

Murray, Horn and Jerome Lowengrub -- were told by Yanowitch that the document was "highly confidential" and that he wanted "to keep it from being disseminated." The three men agreed (not in Schulz' presence) to "hold off" making any photocopy. (Tr. 3269) Amazingly, Peat Marwick made no effort to check the validity of this \$15 million document with the Farmers Home Administration. (Tr. 3529)

E. 1970 Estimated Cost Overruns
(Indictment, ¶15(a))

The specification in Paragraph 15(a) of the indictment was tailored to one of Schulz' grand jury admissions. That admission was virtually the only evidence to support this specification.

Homex also used the percentage-of-completion method to book the portion of the contract price specified as the installation price. As the installation of a housing project progressed, Homex recorded a percentage of the installation price as gross income, and also recorded a percentage of the estimated cost of the total installation.

Schulz' admission concerned the "Christman incident." It was read to the jury at Tr. 2606-10.* In 1970, after the figures for the fiscal year ending July 31, 1970 had been supplied to the auditors, David Christman,** a member of his staff, abruptly informed him of some bad news. It was Christman's job to supply the installation cost estimates and keep them up-to-date. Christman now revealed that he had neglected to keep them up-to-date, that the estimates which he had previously supplied now appeared to be erroneous, and that his new estimates were about \$500,000 higher. Schulz told Christman to delay recording these new estimated cost overruns -- to make the appropriate entries in the new fiscal year, but not to recompute the figures for the past fiscal year. Schulz further admitted that he did not reveal the "Christman incident" to the auditors.

* See Schulz App. 64-66, 70-72.

** The Government did not call Christman, because Christman did not remember the incident. Affidavit of Douglas F. Eaton, March 10, 1977; Schulz App. 136-37.

There was no evidence that Schulz' instruction to Christman was part of any conspiracy with any of the other defendants, or that any of them knew that the booking of the new cost estimates had been delayed. Moreover, Schulz' conduct after the "Christman incident" indicated that Schulz had not acted with criminal intent. That evidence will be discussed below under the heading of Schulz' Defense Case.

F. U.S. Shelter Revenue (Indictment, ¶15(b))

U.S. Shelter, a financing subsidiary of Homex, recorded a \$300,000 fee due from Greater Gulf Coast for finding the Farmers Home commitment. A defendant could be found guilty of this specification only if he knew that the Farmers Home letter was invalid, or knew that the letter was signed after February 28, 1971. (See Tr. 3333) There was no evidence that Schulz knew either of these things.

G. Deferred, General and Administrative Expenses (Indictment, ¶15(c))

This specification related to \$832,000 spent by Homex in connection with the Mississippi plant which was never

built. These expenses covered selecting and obtaining the site, design of the proposed building, and some clearing and draining of the land. The only evidence about this \$832,000 item came from Murray, who said that it was entirely proper. (Tr. 3293-94, 3532)

H. Stock Purchases for Labor Officials
(Indictment, ¶16)

This was the only one of the specifications which did not charge Schulz.

SCHULZ' DEFENSE CASE

Schulz called only one witness, J. Thomas Woods. Woods, a CPA still employed by Peat Marwick, was the supervisor of their Homex audit team. Woods had been embroiled for five years in the civil litigation, where the interests of Peat Marwick and Schulz are completely antagonistic. During these five years, Woods had not spoken to Schulz or Schulz' attorney. (Tr. 4745, 4751) Nevertheless, Woods' testimony proved helpful to Schulz.

A. Defense to ¶13 (Reassignments)

Schulz' defense was that he had relied on the approval of the CPA's -- Professor Mauriello, Murray, Woods and Michael Horn.*

Murray had testified that any reassignments would violate the principles of Homex's method of accounting. He claimed that he knew nothing about the reassignments until December 1971.**

Woods told a different story. Woods testified that, prior to the second offering, he had known of reversals of sales previously reported to the SEC and to the public -- specifically, reassignments of \$1 million worth of modules in a space of less than 3 months -- and that he had not considered this significant. (Schulz Exh. B-20, Tr. 4779-80). In May 1971 Woods wrote in his work papers that "once in a while modules may later be switched to a

* Horn is a partner in Peat Marwick and was Woods' immediate superior. He did not testify. In the civil litigation, after a Rule 34 request for documents was served on Peat Marwick, Horn destroyed at least two of the documents (Tr. 4823-26), raising the distinct possibility that Horn had something to hide.

** Tr. 3448. However, Murray admitted that in March 1971 Schulz gave him a statement of Homex's accounting policies, which said: "The company manufactures modules against specific backlog orders but reserves the right to substitute other orders as conditions require." (Gx 809, Tr. 3449; emphasis supplied)

different project." (Schulz Exh. B-17, emphasis supplied) Woods got this information from Schulz. (Tr. 4786) Schulz also told Peat Marwick that he felt that Homex could wait until the close of the reporting period to select jobs for inclusion in sales. (Tr. 4801-02) Woods felt such a practice would be wrong if done "on a regular basis." (Tr. 4798) Woods thought this was conveyed back to Schulz, but said that his impression may have been based merely on hearsay from Horn. (Tr. 4790)

In short, Schulz made disclosures to Peat Marwick which further explained the reversals noted on the books, but it is not clear what feedback he received. If he received no adverse feedback, he was surely entitled to rely on Peat Marwick's certification. At the worst, if some one did say to Schulz that his (and Mauriello's) opinion about "waiting" was "wrong," this would only indicate that Peat Marwick considered the initial entry on the books to be an "assignment." It would not indicate that a subsequent "reassignment," before the close of the reporting period, was improper. Nobody ever told Schulz any such thing. As for Woods, even after the bankruptcy he did not feel that intra-period "reassignments" were by any means

a serious problem. In fact, Woods reaffirmed his SEC testimony that "whether or not you had it on one contract in September and another contract in January or February, the point is that that wouldn't have had any impact on sales for the seven months ended February 28th." (Tr. 4817)

B. Defense to ¶15(a) (Cost Overruns)

Paragraph 15(a) was a minor specification in relation to the rest of the case. Indeed, the Government conceded in its rebuttal summation that the Christman incident alone "wouldn't bring us here today." (Tr. 5950)

Paragraph 15(a) focused only on the overruns as of July 31, 1970. It is very revealing that the Government made no charge about Homex's treatment of overruns in its later financial statements, even though the overruns mounted to \$2 million, four times the amount that Schulz and Christman had delayed recording. (Tr. 4772-73) The following evidence made it clear why the indictment had been so selective.

Although Schulz' initial delay in recording the overruns was admittedly improper, it occurred after

the first stock offering; before the second offering, the auditors had all the facts about the overruns. Shortly after the Christman incident, Schulz asked Reuben Davis, a Homex attorney, to research whether the Department of Housing and Urban Development would accept claims for such overruns. Davis replied that there was a proper procedure for this, and that "upon the filing of a claim, HUD sets aside a reserve pending the resolution of a claim." (Schulz Exh. E-1) Schulz then notified HUD of claims for additional costs on five projects. (Schulz Exhs. E-2 through E-6). There was evidence* that as late as February 8, 1971 Schulz was still uncertain about the collectability of the overruns. However, soon after this date Schulz received HUD's replies.** Although these replies were

* Gx 598 at p. 6, a memo Schulz wrote two weeks before Peat Marwick was engaged.

** Schulz Exhs. E-7 through E-11. Despite their date, the fact that they were received after Gx598 was shown by the contents of another memo, Gx 456 at p. 4.

non-committal,* Schulz and Peat Marwick found them very reassuring.** Moreover, Peat Marwick verified that Homex had a good history of collection of past overruns. (Schulz Exh. B-7). Based on all this, and a thorough review of the facts on each project, Peat Marwick said it was proper to record both the 1970 and 1971 overruns as accounts receivable. (Schulz Exhs. B-13, B-14, B-21, B-24, B-26, B-27; Tr. 4760)

* Subsequently, on the first of the five projects, HUD paid 85% of the overruns claimed by Homex. (Compare Schulz Exhs. B-15 and B-21 with E-7)

** Peat Marwick's work papers stated: "HUD letters were also examined which indicated their intention of paying for the added costs." (Schulz Exh. B-7)

POINT I

SCHULZ' GRAND JURY TESTIMONY WAS MADE IN CONNECTION WITH AN OFFER TO PLEAD GUILTY, AND SHOULD HAVE BEEN SUPPRESSED PURSUANT TO CRIMINAL RULE 11(e)(6).

This case presents a straightforward issue under Rule 11(e)(6) of the Federal Rules of Criminal Procedure. This is a new Rule which took effect on August 1, 1975. To the best of my knowledge, this Court has not had occasion to discuss the Rule in any previous case. Other Circuits have given full effect to the Rule's broad language excluding all statements made in connection with an offer to plead guilty. United States v. Herman, 544 F.2d 791 (5th Cir. 1977); United States v. Brooks, 536 F.2d 1137 (6th Cir. 1976); United States v. Smith, 525 F.2d 1017 (10th Cir. 1975). The Rule marks a change from the previous law in this Circuit; cf. United States v. Zane, 495 F.2d 683, 693-94 (2d Cir.), cert. denied, 419 U.S. 895 (1974), decided before the Rule was promulgated.

The Rule reads as follows:

"Inadmissibility of Pleas, Offers of Pleas, and Related Statements. Except as otherwise provided in this paragraph, evidence of a plea of guilty, later withdrawn, or a plea of nolo contendere, or of an offer to plead guilty or nolo contendere to the crime charged or any other crime, or of statements made in connection with, and relevant to, any of the foregoing pleas or offers, is not admissible in any civil or criminal proceeding against the person who made the plea or offer. However, evidence of a statement made in connection with, and relevant to, a plea of guilty, later withdrawn, a plea of nolo contendere, or an offer to plead guilty or nolo contendere to the crime charged or any other crime, is admissible in a criminal proceeding for perjury or false statement if the statement was made by the defendant under oath, on the record, and in the presence of counsel."(Emphasis supplied)

In the case at bar the following facts are undisputed:

1. The plea agreement required Schulz to testify before the grand jury.
2. Schulz was required to testify before there was any available text of the conspiracy count to which he was offering to plead guilty.
3. Schulz was required to testify before his proposed plea could be submitted to any judge.

4. Schulz' grand jury testimony was given at a time when the plea agreement was considered in effect by both parties, and when Schulz had no thought of withdrawing from the plea agreement.

Therefore, it would seem obvious that Schulz' statements before the grand jury were statements made "in connection with" his offer to plead guilty. The burden should have been on the Government to show why the clear language of Rule 11(e)(6) was somehow inapplicable. Schulz' motion was further supported by:

- A. A detailed analysis of the facts.
- B. The legislative history of the Rule.
- C. Authorities which have discussed the Rule.
- D. Decisions which discuss the Constitutional problems in Schulz' type of situation.

These four topics will now be discussed in detail. After that, Judge Frankel's reasoning will be analyzed.

A. The Facts

Many of the facts were undisputed, and the Court did not reject a single one of the facts alleged by Schulz. Prior to giving his grand jury testimony, Schulz met with

Assistant United States Attorney MacDonald on nine occasions. On each of the first five occasions, in January and February of 1976, MacDonald gave the Miranda warnings to Schulz. On the next four occasions, in June and July of 1976, the warnings were not given. (MacDonald aff., ¶ 8, ¶10; Schulz App. 28-29)

The two sets of meetings had completely different purposes. In the first set of meetings, Schulz was trying to assure the prosecutor that there were no grounds for indicting him. The purpose of the second set of meetings was plea bargaining.

Between February and June, as one might have guessed, several important events had occurred. In March MacDonald announced that he would recommend that Schulz be indicted.* At this point, Schulz' attorney, George Miller of the Pennsylvania bar, instructed Schulz to stop talking.** On May 11 Miller met with MacDonald for the first time in person. MacDonald said he wanted Schulz to plead guilty and be a witness for the Government. MacDonald offered to consider more lenient treatment for Schulz, including the possibility of complete immunity, if Schulz could incriminate William Murray of Peat Marwick.*** The

* Tr. 2009-10; Schulz App. 99-100.

** Miller aff. ¶4, Schulz App.16-17 ; Tr. 2010-11, Schulz App. 100.

*** Miller aff. ¶7, Schulz App.17; Tr. 2012, Schulz App. 102.

Government was particularly interested in any possible evidence against Murray with regard to Homex's three land sales. Unfortunately for Schulz, he had insufficient knowledge about the land sales, so the idea of total immunity was dropped.*

In June and July, after a four-month break, Schulz resumed meeting with MacDonald, this time for the purpose of plea bargaining. The Government continued to express interest in other information concerning Murray, Horn and other possible defendants; Schulz provided it, and the Government wanted him to repeat it before the grand jury.** The eventual plea agreement was proposed orally and tentatively on July 3 and was concluded on July 15.*** This plea agreement is reproduced at Schulz App. 5-7.

It provided in pertinent part as follows:

On the understandings specified below, the United States will accept a guilty plea from Edwin J. Schulz to one count of an Indictment charging a violation of 18 U.S.C. §371....

* Miller aff. ¶7-8, Schulz App. 17.

** Miller aff. ¶8,10, Schulz App. 17-19.

*** Tr. 2018-19, Schulz App. 108-09.

The understandings are that Mr. Schulz shall truthfully disclose all information with respect to the activities of himself and others concerning all matters about which this Office inquires of him, and, further, shall truthfully testify before the Grand Jury and/or at any trial or other court proceeding with respect to any matters about which this Office may request his testimony.

At the time of this agreement, and at the time of Schulz' grand jury testimony, there was no text of the conspiracy count, and no commitment as to exactly what it would charge.* Miller asked if Schulz could waive indictment and offer his guilty plea before a judge prior to testifying in the grand jury; the Government declined to allow that procedure.**

It is undisputed that the June and July meetings were plea bargaining sessions, and that their main purpose was to convince Schulz to plead guilty and to testify as a Government witness. It is also undisputed that Rule 11(e)(6) was never mentioned to Schulz. Miller was a highly respected civil litigator, but he had a limited acquaintance

* Tr. 2014-15; Schulz App. 104-05.

** MacDonald aff. ¶13; Schulz App. 33.

with criminal law.* He did not know about Rule 11(e)(6), but he did know about Rule 408 of the Federal Rules of Evidence, concerning statements made in compromise negotiations.** He did not believe that the Government would seek to use the statements made by Schulz in the course of the plea negotiations, unless Schulz gave false or incomplete information. He never focused on the possibility that Schulz might withdraw from the plea agreement. If he had, and if the Government had stated its present position, Miller might well have advised Schulz not to enter into the plea agreement.*** MacDonald, an experienced and highly respected prosecutor, knew about Rule 11(e)(6), but simply did not think about it one way or the other with respect to his discussions with Schulz.

Nevertheless, the Government contends that somehow Schulz must have known that his statements, during the

* Miller aff. ¶1; Schulz App. 15.

** Miller aff., ¶17; Schulz App. 21.

*** Miller aff., ¶15-16; Schulz App. 20.

plea bargaining sessions and before the grand jury, could be used against him if the plea agreement fell through.

The record refutes the Government's contention. When Schulz was before the grand jury he fully intended to plead guilty.* He was under no illusion that his testimony might persuade the grand jury not to indict him.** He thought of himself simply as a Government witness.*** MacDonald asked Schulz to try to give "Yes" or "No" answers before the grand jury.**** MacDonald even went to the unnecessary and improper extreme of getting Schulz to promise to the grand jury that he would plead guilty to their indictment.***** These facts, of course, were not revealed to the trial jury, but they caused Schulz' statements to be especially effective against him at trial. Schulz answered with a tame "Yes" to one leading

* Judge Frankel found this fact at Tr. 2037; Schulz App.127.
See Tr. 2022; Schulz App.112.

** Tr. 2021; Schulz App.111.

*** His lawyer was not present outside the grand jury room; instead, he remained in Pennsylvania.
Miller aff. ¶11; Schulz App.19.

**** Schulz aff. ¶10; Schulz App.12.

***** Schulz App.52.

question after another, and did not resist the nuances in the prosecutor's questions.

No one ever mentioned the possibility that Schulz might withdraw his offer to plead guilty. He never considered that possibility until well after his grand jury appearance.* He was told of only two possibilities that his testimony could be used against him:

1. If he were to commit any further crimes.
2. If he were to give false, incomplete or misleading information (in the prosecutor's judgment).

Schulz had no concerns about the first possibility. The second possibility was mentioned to him repeatedly: by MacDonald on July 3, ** by the plea agreement, and by MacDonald before the grand jury.

The plea agreement stated:

"It is further understood that Mr. Schulz must at all times give complete, truthful and accurate information and testimony and must not commit any further crime whatsoever. Should Mr. Schulz commit any further crimes or should it be judged by this Office that Mr. Schulz has

* Schulz aff. ¶10; Schulz App.13.

** Miller aff. ¶15; Schulz App. 20.

given false, incomplete or misleading testimony or information, or has otherwise violated any provision of this agreement, this agreement shall be null and void and Mr. Schulz shall thereafter be subject to prosecution for any federal criminal violation of which this Office has knowledge, including, but not limited to, perjury and obstruction of justice. Any such prosecutions may be premised upon any information provided by Mr. Schulz, and such information may be used against him."
(Emphasis in the original)

The very next paragraph said:

"No additional promises, agreements and conditions have been entered into other than those set forth in this letter and none will be entered into unless in writing and signed by all parties."

The Government drafted the plea agreement, and it should not be permitted to claim, contrary to the last sentence, that there was an additional agreement or condition, namely an understanding that Schulz' statements could be used against him in any circumstances other than those specified in the agreement.

When Schulz appeared before the grand jury, he was not given all of the customary warnings. In view of the plea agreement, it would have been false to tell Schulz that "anything you say can be used against you." Instead,

he was told of only one circumstance in which his statements could be used against him. MacDonald had the plea agreement in front of him, and the following took place:

"Q. And you understand further that waiving that right and giving answers in the ordinary case, subjects the person giving the answers to the possibility that they can be used against him in a later criminal proceeding?

A. Yes.

Q. You understand that under certain events, which I will describe in a moment, your answers today can be used against you in some later criminal proceeding as well?

A. Yes.

Q. So, when you make answers today and waive your right of silence, you appreciate the possibility that some day those answers can be used against you?

A. Yes.

* * *

Q. You understand that should you at any time in the course of your cooperation, give less than the whole truth by either an omission or deliberate false statement, that all of the immunity which you have been assured, falls away and you're subject to full prosecution for all of the offenses which I just referred to?

A. Yes."

(Schulz App. 50-53 , emphasis supplied)

After the plea agreement was entered into, the Government never claimed that Schulz (1) committed

"any further crimes," or (2) gave "false, incomplete or misleading testimony or information." Accordingly Schulz' statements should not have been used against him.

B. The Legislative History of Rule 11

The 1974 and 1975 Amendments to Rule 11 are the result of a thorough study of the entire subject of plea bargaining and "cooperation." Rule 11(e)(6) was the subject of particularly extensive consideration in Congress. One of Congress' main purposes was to give defendants more incentive to plead guilty and "cooperate" with the prosecutor.*

At the same time, Congress recognized that there was a danger of abuse of plea discussions and agreements. Plea discussions exert a strong pressure against a suspect's Fifth Amendment rights. The Government can threaten him with indictment for many crimes, and then offer to accept a plea to one crime, in return for "cooperation." By this means, the Government not only gets information against

* The Advisory Committee Notes, in listing the benefits of plea agreements, had stated: "Finally, a plea agreement may also contribute to the successful prosecution of other more serious offenders."

others, but it also gets admissions from the suspect. Such admissions would tend to "lock" him into the proposed plea, before the plea is ever presented to a judge. Rule 11(e)

"is designed to prevent abuse of plea discussions and agreements by providing appropriate and adequate safeguards." *

A number of the safeguards come into play when the defendant appears before a judge. But one key safeguard takes effect prior to any appearance before a judge; that is the "security" provided by Rule 11(e)(6):

"...free communication is needed, and security against having an offer of compromise or related statements admitted in evidence effectively encourages it." **

What is this new and additional "security"? In plain English, the new Rule gives suspects the right to "back out." Rule 11(e)(6) comes into play only in four situations:

- * Advisory Committee Notes to Rule 11(e), emphasis supplied.
- ** Advisory Committee Notes to Rule 410 of the Federal Rules of Evidence, emphasis supplied. Rule 410, as originally drafted, was virtually identical to the present Rule 11(e)(6).

1. The plea discussions break down, and no plea agreement is reached.

2. A plea agreement is reached, but one of the parties does not go through with it. (This could happen either because a party claimed a violation of the agreement's terms, or because, as happened in the case at bar, the defendant exercised his absolute right not to plead guilty.)

3. A plea agreement is reached, but the Court refuses to accept the plea. (This could happen either because the Court found the agreement inappropriate, or because the Court found the defendant's allocution inadequate.)

4. The plea is made and accepted, but later withdrawn.

The Rule makes no distinction among these situations. Also, the Rule makes no distinction based on whether the statements were made before or after the offer to plead guilty. If the Rule's drafters had wanted to make such a distinction, they would have used narrow terms such as "plea discussions" or "statements made prior to a plea agreement." But they did not. Instead, they used the

broad language, "statements made in connection with... any of the foregoing...offers."

There is clear evidence that the use of this broad language was deliberate. First, the drafters had before them the text of Illinois Supreme Court Rule 402(e).^{*} The Illinois rule, adopted in 1970, used the words "neither the plea discussion nor any resulting agreement." The drafters of Rule 11(e)(6) did not use this language, even though they used the word "discussions" in Rule 11(d) and Rule 11(e)(1). Second, Congress contemplated that statements might be made after a plea agreement, and pursuant to its terms. The House Committee Notes to Rule 11(e) state:

"...It is apparent, though not explicitly stated, that Rule 11(e) contemplates that the plea agreement may bind the defendant to do more than just plead guilty or nolo contendere. For example, the plea agreement may bind the defendant to cooperate with the prosecution in a different investigation. The Committee intends by its approval of Rule 11(e) to permit the parties to agree on such terms in a plea agreement."

* Ill. Rev. Stat. 1973, ch. 110 A, §402(e). This is the only state rule mentioned in the Advisory Committee Notes to Rule 11(e)(6).

It may well be that, in particular cases, the Government, at least as an initial bargaining position, would not want to make a plea agreement if the suspect could make a "cooperative" statement and then back out. The new Rule has not left the Government in an unfair quandary. The Government has its choice of two simple and equitable ways to proceed:

1. The Government could ask the suspect to waive the rights given to him by Rule 11(e)(6).

2. The Government could take the suspect's statement "under oath, on the record, and in the presence of counsel." Pursuant to the last sentence of Rule 11(e)(6), such statements are admissible in a criminal proceeding for perjury or false statement.

The Government made no attempt to follow either of these two procedures with Schulz.*

* Interestingly, the Government did follow the second procedure with Murray and Horn, the two Peat Marwick partners, although they were not engaged in plea bargaining. Before they answered questions in the grand jury, they were questioned at great length in the prosecutor's office. These sessions were under oath and stenographically recorded. They were considered proceedings "ancillary" to the grand jury's investigation. The attorneys for Murray and Horn requested this procedure so that they could be present during the questioning. These sessions were well before Schulz' July 16 testimony. (See Tr. 3508-10)

C. Authorities Which Have Discussed the Rule

Rule 11(e)(6) was discussed at length in United States v. Herman, 544 F.2d 791 (5th Cir. 1977). The Fifth Circuit stated:

...Having embarked on the road that permits plea bargaining, the government should be most careful lest it be accused of bad faith in throwing open to the trial matters that the accused thought were not to be used against him or her.

...if we were to construe the "in connection with" standard more narrowly, sophisticated prosecutors might sometimes use the rule as a trap for the unwary.

(544 F.2d at 797)

In United States v. Albano, 414 F.Supp. 67, 69 (S.D.N.Y. 1976), Judge Pierce noted, as an alternative ground, that Rule 11(e)(6) applied to a letter written by the defendant to the Court after he entered a guilty plea and before the Court reversed its initial decision to accept it.

I have found no case dealing with the Rule's applicability to grand jury testimony. However, Judge Weinstein's treatise assumes without discussion that the Rule does apply to statements before a grand jury, as long

as they meet the other defining terms in the Rule.*

Judge Weinstein's views may be entitled to special weight because he was a member of the Advisory Committee on the Federal Rules of Evidence; that Committee's Rule 410, as originally promulgated, was virtually identical to the eventual wording of Rule 11(e)(6).

D. Decisions Discussing the Constitutional Problems

The Government's restrictive interpretation of the Rule should be rejected for the additional reason that it creates serious Constitutional problems. These problems were discussed by the Eighth Circuit and the Supreme Court in Mobley ex rel. Ross v. Meek, 531 F.2d 924 (8th Cir.); rev'd sub nom. Hutto v. Ross, 97 S.Ct.202 (1976). That case arose on habeas corpus from a state conviction. Accordingly, Rule 11(e)(6) was not directly involved, but rather two Constitutional tests:

* 2 Weinstein's Evidence, ¶410[07], pages 410-41 to 410-42. Judge Weinstein's hypothetical presents a "gray area," but Schulz' case is more compelling in every respect. In the hypothetical, as in United States v. Zane, supra, there was a dispute as to whether the defendant was in fact plea bargaining. In the case at bar, there is no such dispute.

1. Whether the confession was "obtained by any direct or implied promises, however slight," Bram v. United States, 168 U.S. 532, 542-43 (1897); see Brady v. United States, 397 U.S. 742, 753 (1970); and

2. Whether the "evidence of guilt [was] induced from a person under a governmental promise of immunity," Shotwell Mfg. Co. v. United States, 371 U.S. 341, 347 (1963); see Judge Mansfield's dissent in United States v. Nussen, 531 F.2d 15, 23 (2d Cir.), cert. denied, 97 S.Ct. 112 (1976).

The facts were that Ross gave a written confession, in the presence of his counsel, approximately two weeks after a plea agreement had been concluded. Later Ross backed out of his plea agreement. At his trial, the prosecution introduced his confession.

The Eighth Circuit granted a writ of habeas corpus, and held as follows:

"...the confession was given as a result of the plea bargain and was therefore involuntary under all the circumstances." (531 F.2d at 927)

In the Supreme Court, Justice Stewart agreed with this reasoning. The other Justices reversed, but their opinion

gives no comfort to the Government in the case at bar.

Their opinion relied on the following facts:

"...it [the confession] was made subsequent to an agreed upon plea bargain that did not call for such a confession. ... counsel made it clear to respondent that he could enforce the terms of the plea bargain whether or not he confessed. The confession thus does not appear to have been the result of 'any direct or implied promises' or any coercion on the part of the prosecution, and was not involuntary. Bram v. United States, supra, 168 U.S. at 542-543." (97 S.Ct. 202, 203-204, emphasis supplied).

In the case at bar, however, the plea agreement specifically required Schulz to testify before the grand jury. He could never have enforced the terms of the plea bargain if he had invoked his Fifth Amendment privilege before the grand jury. MacDonald made it clear to the grand jury that Schulz was not testifying voluntarily:

"Q. You are appearing here today, are you not, under certain assurances which are embodied in a document numbered 88296 to 298 [the plea agreement]?"

A. Yes.

Q....this embodies the scope of the understandings that have induced you to appear here and to waive your privilege of silence?

A. Yes." (Schulz App.50-51, emphasis supplied)

The Government's "inducement" included a promise of valuable, though partial, immunity. Schulz' guilty plea

was limited to one count, but that was not all. On July 3 Schulz and Miller persistently asked what that count would charge against Schulz. Although MacDonald would not limit himself, he mentioned only three potential specifications against Schulz: (1) the Christman incident, (2) the use of "File 2" and (3) the \$832,000 billing.* Moreover, MacDonald said that the Government would be satisfied if Schulz' guilty plea allocution admitted guilt only as to the Christman incident. (Tr. 2013-15, Schulz App. 103-05; Miller aff. ¶10, Schulz App. 18-19)

E. Judge Frankel's Reasoning

Judge Frankel denied Schulz' motion on two grounds:

1. That the motion's reading of Rule 11(e)(6) was "unacceptable" -- that it put all the benefit on one side, that it would be unfair to allow Schulz to "back out," and that there might be "evil consequences" for other defendants. (Tr. 2037-40; Schulz App. 127-130)

* Needless to say, Schulz was shocked when the indictment charged him with the land sales and the Mississippi sale. This was the main reason he decided not to plead guilty. (Tr. 2033, Schulz App. 123)

2. That even if Rule 11(e)(6) was applicable, the plea agreement in this case "contemplated" that Schulz' statements could be used against him if he "breached" the agreement, that is, if he exercised his right to go to trial. (Tr. 2041; Schulz App. 131)

We shall now discuss those two rationales in sequence.

Judge Frankel's first ground shows an antipathy to the basic philosophy of the Rule. As discussed above under Legislative History, the whole point of the new Rule is to give defendants a new type of "security," to allow them to "back out" from statements which they previously made.

The Court was incorrect when it said that Schulz would get all the "benefits" if his motion were granted. In fact, the Government would have still retained three significant benefits:

1. It got Schulz' grand jury testimony against Murray and Horn, which it very much wanted at the time, although ultimately Murray and Horn were not indicted.

2. It got the indictment of Schulz. This would not have been a "sure thing" except for Schulz' appearance, including the elicitation of his "promise" to the

grand jury to plead guilty to their indictment,* and his crucial admission about the "Christman incident."

Christman, who was not called before the grand jury, did not remember the incident. (Schulz App. 136-137)

3. It got valuable "leads" from Schulz, and it was free to use them against him and the other defendants.

Unless the Government seeks an explicit waiver, or takes the defendant's statement "under oath, on the record, and in the presence of counsel," it is entitled to no further "benefits" if the defendant exercises his Constitutional right to "back out" of a plea agreement -- this is Congress' policy judgment. Congress decided that, by allowing potential defendants to make such statements and then "back out," in the long run the Government will receive more information, more "cooperation," and hence more benefits on balance.

Judge Frankel was bothered that such a policy might lead to "evil consequences" for other prospective defendants who might be indicted on the basis of the "cooperating" witness' grand jury testimony. Here, the most important point to keep in mind is that no one has ever contended that

* Schulz App. 52.

Schulz gave any false information against any other person. As to Judge Frankel's concern about other possible situations, there is no reason to believe that Congress was unaware that plea bargaining pressures may lead some defendants to "cooperate" by accusing others falsely. These pressures have existed long before the new Rule. The remedies will continue to be the traditional remedies, particularly cross-examination of witnesses who have made plea bargains.

Judge Frankel's second ground was that, even if Rule 11(e)(6) was applicable, the plea agreement "contemplated" that the Government could use Schulz' statements against him if he "breached" the agreement by refusing to plead. In effect, the Court was saying that if Rule 11(e)(6) applies, then its provisions were waived. The facts in this case do not support a finding of a waiver.

No one can waive a right unless he knows of its existence. See Brewer v. Williams, 437 S.Ct. 1232, 1242 (1977), citing Johnson v. Zerbst, 304 U.S. 458, 464 (1938). As we have demonstrated above at pages 32-37, Schulz did not know about Rule 11(e)(6), and also had no idea that

the Government would seek to use his statements if he withdrew his offer to plead guilty.

We have previously discussed the following crucial portion of the plea agreement:

Should Mr. Schulz commit any further crimes or should it be judged by this Office that Mr. Schulz has given false, incomplete or misleading testimony or information, or has otherwise violated any provision of this agreement, this agreement shall be null and void and Mr. Schulz shall thereafter be subject to prosecution for any federal criminal violation of which this Office has knowledge, including, but not limited to, perjury and obstruction of justice. Any such prosecutions may be premised upon any information provided by Mr. Schulz, and such information may be used against him. (Schulz App. 6) (Emphasis in the original)

As we have previously noted, after this agreement was entered into, the Government never claimed that Schulz (1) committed "any further crimes," or (2) gave "false, incomplete or misleading testimony or information." However, Judge Frankel made much of the clause which read "or has otherwise violated any provision of this agreement." Judge Frankel said that the agreement had an implicit provision that Schulz actually plead guilty, and that Schulz had "violated" this implied provision by failing to plead guilty. (Tr. 2035, Schulz App. 125)

This is a tortured reading of that catch-all clause. Although it is hard to know exactly what was intended by the clause, there is one situation to which it could legitimately apply. If Schulz pleaded guilty to one count, but refused to testify at the trial of the other defendants, then the clause could have been invoked.

But it was unfair to invoke the clause when all Schulz did was to exercise his constitutional right to a trial. The plea agreement did not, and could not, require Schulz to plead guilty. All it said was that on certain understandings the United States would "accept" a guilty plea to one count.

One cannot overemphasize that the final decision on every guilty plea rests with the Court. Suppose that a defendant made a plea agreement, went before a judge, but made an unsatisfactory allocution. May the Government argue that the defendant made the unsatisfactory allocution deliberately, and therefore "violated" an implicit provision that he give the "right" answers at his allocution?

POINT II

CERTAIN OF THE INDICTMENT'S SPECIFICATIONS AGAINST SCHULZ WERE NOT SUPPORTED BY SUFFICIENT EVIDENCE, AND SHOULD HAVE BEEN WITHDRAWN FROM THE JURY'S CONSIDERATION.

Schulz' conviction should be reversed for the same reason that this Court reversed Scansaroli's conviction in United States v. Natelli, 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976), namely, because the jury may well have convicted Schulz solely on the basis of specifications which were not supported by sufficient evidence.*

Each count contained the same eight specifications, seven of which charged Schulz. This brief has demonstrated, in its Statement of Facts, that none of the specifications against Schulz was supported by sufficient evidence except

* This type of problem was not new with Natelli. It also arose in Yates v. United States, 354 U.S. 309, 312 (1957) (conspiracy with two objectives, one of which was barred by statute of limitations); United States v. Jacobs, 475 F.2d 270, 281-84 (2d Cir.), cert. denied, 414 U.S. 821 (1973) (conspiracy with two objectives, one of which was not supported by sufficient evidence); United States v. Guterma, 281 F.2d 742, 747-48 (2d Cir.), cert. denied, 364 U.S. 871 (1960) (failure to file Form 4 report for two sales, one of which was not supported by sufficient evidence); United States v. Borelli, 336 F.2d 376, 386 (2d Cir. 1964) (conspiracy with two phases, "it would be best to have the jury determine whether he became a party to both phases").

the two contained in Paragraph 13 and Paragraph 15(a). Those two were relatively minor specifications and Schulz put in substantial defenses to each of them. There is a very real possibility that the jury did not convict Schulz on the basis of either of these specifications.

The jury may well have convicted Schulz on the basis of the specifications concerning the land sales (Paragraphs 10, 11 and 12) or the Mississippi sale (Paragraph 14). They were urged to do so by the prosecutor's summation and rebuttal summation. (Tr. 5631-32, 5922-23) The Court instructed them that they could convict Schulz on the basis of any one of the specifications against him. With respect to the land sales the Court, both times over objection, allowed an improper rebuttal summation, and then in its charge misstated Schulz' contention. With respect to the Mississippi sale, which was the most serious specification in the case, the Court came tantalizingly close to deciding to give Schulz something approaching a withdrawal instruction,* but did not do so.

* "I will tell the jury to focus on the issues. That Mr. Schulz is not involved, by and large, with the Greater Gulf Coast business...." (Tr. 5521, Schulz App.155.)

Schulz did everything to make the sufficiency problem clear to the trial court, and did much more than Scansaroli did in the Natelli case.

At the close of the Government's case, Schulz' counsel cited Natelli and said he wanted to make separate motions addressed to Paragraphs 10 through 16 individually. (Tr. 3569-72, Schulz App. 150-53) The Court stated:

"I don't grant Rule 29 motions as to parts. *** I am not going to rule on which paragraph does or does not embrace which defendant at this time."
(Tr. 3571, Schulz App. 152)

This ruling was erroneous; the Court should have considered the sufficiency of the evidence with respect to each challenged specification. In Natelli, this Court acknowledged that in Rule 29 "[n]o provision is made for a motion to withdraw one of two specifications in a single count on the ground of insufficiency." (527 F.2d at 329) Nevertheless, this Court found that "there should have been a directed verdict for a defendant [Scansaroli] on one of the specifications for insufficiency of evidence," and that Scansaroli had made it clear enough that he wanted

"a judgment of acquittal or some equivalent" on the unsupported specification. (527 F.2d at 325 and 329)

Three days later, Schulz pursued the point by making, in writing, a more detailed motion and two supplemental requests to charge. The motion asked for "separate dismissals of the following specifications for insufficiency of evidence, and withdrawal of the following specifications from jury consideration." (Schulz App.138-39) The requests to charge concerned two separate issues: (1) withdrawal of the same specifications, and (2) jury unanimity. (Schulz App. 140-41)

The Government then submitted a brief (Schulz App.142) which will be analyzed below since Judge Frankel adopted the Government's position (Tr. 5520-21, Schulz App.154-55)

The Government's position was that Schulz' motions and requests should be denied except for an instruction on jury unanimity limited to Count Two, the false statement count. (Since Schulz was convicted on all counts, he is not raising an appellate issue about the unanimity charge; however, it made no sense to limit Natelli's comments on unanimity merely to false statement charges.)

As to the sufficiency of the evidence, the Government contended that Judge Frankel had been correct, and that it would be improper to consider each paragraph separately. If Judge Frankel had changed his mind, the Government stated*that it was prepared to argue orally that the evidence supported each of the paragraphs. No such argument ever took place, because Judge Frankel's view was that if there was sufficient evidence against Schulz on one specification, then he had to give the jury all the specifications which charged Schulz.

The Government's brief made a simplistic attempt to distinguish Natelli. It said that the specifications in Natelli charged "disparate and separable false statements," and that the specifications in the case at bar charged a "unified scheme."**Not only did Natelli make no hint of such a distinction, but it cited Yates and Jacobs, which charged conspiracies that were far more "unified" than the conspiracy and scheme alleged in the case at bar.

The Government found great comfort in the facts that all of the counts incorporated a scheme to defraud, and that

* Schulz App. 143.

** Schulz App. 145.

one of them charged a conspiracy to scheme to defraud. Therefore, the Government claimed, it only had to prove that each defendant "entered the conspiratorial agreement" or "devised or intended to devise such a scheme." * This of course begs the question, which is, what was the content of the agreement or scheme?

To prove a fraud scheme, the Government must prove at least one misrepresentation, and the only misrepresentations that were charged were contained in Paragraphs 10 through 16. The Court so instructed the jury at Tr. 6007-08. ** Yet the Government's brief asserted that it need not specify or prove "the particular means" by which the agreement or fraud scheme was carried out. *** (Paragraphs 10 through 16 were entitled "The Means by Which the Fraud Scheme Was Carried Out.") A similar argument was made in Natelli, where the Government characterized the specifications as "means for committing the single crime"; this Court, while not disputing that characterization, held that it was of no assistance when the problem is insufficient

* Schulz App. 145-46.

** Schulz App. 167-68.

*** Schulz App. 145.

evidence on one of the specifications.*

Paragraphs 10 through 16 were not gratuitous verbiage. Without them, the indictment would have failed to allege an offense. In each specification, the Government took pains to charge specific defendants. For example, only three defendants were named in Paragraph 16, and only four in some of the other paragraphs. Obviously, the Government hoped to introduce sufficient evidence to support each of these charges. It failed to do so. In its charge to the jury, the Court described these specifications paragraph by paragraph, and correctly stated that they were "the essence or the heart" of the alleged scheme. (Tr. 5979-91) The Court did note which defendants were charged in each specification, but this was not enough. The point was not merely whom the

* 527 F.2d at 329. This Court also said that it might be the better practice to allege such "means" in separate counts.

Government had charged, but which charges had been supported by enough evidence to present them to the jury. Accordingly, the Court should have withdrawn from the jury's consideration all of the specifications against Schulz except Paragraphs 13 and 15(a). Instead, the Court instructed the jury that they could convict Schulz on the basis of any one of the specifications charged against him. (Tr. 6007-08, Schulz App.167-68)

The danger of a conviction based on insufficient evidence was especially acute with respect to the land sales (Paragraphs 10, 11 and 12) and the Mississippi sale (Paragraph 14), because the prosecutor's summation and rebuttal summation specifically argued that those specifications had been proven against Schulz. (Tr. 5631-32, 5922-23)* Moreover, the Government's argument on the land sales, roping in Schulz for the first time only on rebuttal, was flatly contrary to the evidence. Schulz' objection to this was overruled. See page 7, above.

* Schulz App. 159-62.

The Court's charge made Schulz' exposure on the land sales even more unfair. Perhaps the most thoroughly proven part of the case was the secret oral guarantees in connection with the three land sales. To prove these guarantees, the Government called eight witnesses,* including a physician and two attorneys. It is impossible for the cold record to convey the total believability of these eight witnesses, and the impact they had on the jury. Not one of these witnesses ever mentioned Schulz' name. Not one of them was cross examined by Schulz' counsel. The summation by Schulz' counsel never disputed that there were guarantees, and simply pointed out that there was no evidence that Schulz knew about them.

Nevertheless, Paragraphs 10, 11 and 12 went to the jury. They charged Schulz, along with three other defendants, with arranging all three land sales at artificially high prices that were induced by guarantees, and with fraudulently concealing those guarantees from the SEC. The Court's charge, after directing the jury's attention to these specifications, stated:

* Dr. Morris Shapiro, Donald Barbato, Caesar Falcone, Gerald Beckerman, Harold Wynn, William Grago, Bernard Frank, and Peter Thun.

"Insofar as prosecution witnesses have testified to facts that appear to support those accusations [¶¶ 10-12], the defendants contend, among other things, that at least many of those witnesses must have testified falsely for reasons of their own, such as a hope for freedom for themselves from prosecution by providing these defendants as targets for prosecution instead of themselves." (Tr. 5981-82, Schulz App. 165-66, emphasis supplied)

Schulz' attorney was completely surprised by this, and at the next recess he objected vigorously. The Court refused to correct the misstatement of Schulz' contentions. (Tr. 6026-27, Schulz App. 169-70)

Thus Schulz was roped into the "land sale" specifications on insufficient evidence and a spurious argument first raised in rebuttal summation. Then, just before the jury began to deliberate, Schulz was saddled with the defense of his co-defendants, namely, that "at least many" of the eight witnesses had deliberately lied.

The resulting verdict against Schulz suffers from the same infirmities as the verdict against Scansaroli, which this Court reversed with the following words:

" * * * The verdict then becomes ambiguous, for the jury could have rejected the specification which the appellate court holds sufficiently proved, and have convicted only on the specification held to be insufficiently proved. In that event, there seems to be no alternative to remand for a new trial."
(527 F.2d at 325)

CONCLUSION

The judgment of conviction against the defendant Schulz should be reversed, and a new trial ordered.

Dated: May 9, 1977

Respectfully submitted,

DOUGLAS F. EATON

Attorney for Appellant

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745 Fifth Avenue

New York, New York 10022

STATE OF NEW YORK
COUNTY OF NEW YORK SS.:

DOUGLAS F. EATON, being duly sworn, says:

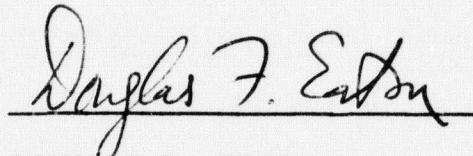
1. On May 9, 1977, I served a copy of the Brief for Appellant Edwin J. Schulz and a copy of the Appendix to said Brief on each of the attorneys for the other parties, as follows:

A. I served the United States Attorney's Office and Patterson, Belknap, Webb & Tyler by hand.

B. I served the following attorneys by mail:

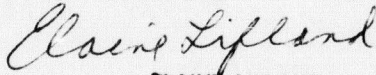
Ford Marrin Esposito Witmeyer & Bergman
25 Broadway
New York, N. Y. 10004

Hawkins Delafield & Wood
67 Wall Street
New York, N. Y. 10005



DOUGLAS F. EATON

Sworn to before me
this 9th day of May, 1977



ELAINE LIFLAND
Notary Public, State of New York
No. 24-4640450
Qualified in Kings County
Commission Expires March 30, 1979